The MORTGAGE BANKER

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Measuring the Future in Appraising Income Producing Properties

It all comes down to a question of how much retail business or rental demand develops at any given site

TO what extent should appraisers attempt to predict the future? How should they treat their opinions in reports? And, more specifically, what are the answers when you're appraising purely income producing properties such as stores, apartments and office buildings?

Such an appraisal involves the estimation of the present worth of the future net income reasonably to be expected from a property, says Albert Keidel, Jr., of Baltimore.

It is difficult to think of any phase of such an appraisal that does not require some forecast of future events, he declares, and goes on from there to say:

"The value of any property will be determined by the *gross volume of the retail business that can be done at the location*. If it is an apartment house, office building or hotel, *the volume of demand for rental space at that location*—and nowhere else—is the determining factor. In other words, *what will be the future consumer demand for a store or for living space at this site?* Future rents and extent of vacancies are the *measures of such demand*.

"The appraiser then asks himself: 'What factors can affect this demand? What can happen in the future that will increase or decrease that consumer demand? What is the origin and nature of the past and present demand which have produced today's tenants and values?'

"In seeking an answer the appraiser must consider both local and foreign factors. By local is meant the metropolitan area and the particular section under consideration in that metropolitan area. It is here that he will discover most justification for a prediction of value trends. The foreign influence, that is national and international factors which may affect local real estate values, are obviously less susceptible to any sort of accurate forecast.

> ***"WE all recognize this (decentralization which is taking place in our large metropolitan centers). The causes for it are fairly obvious. However, it is a relatively recent development; and I doubt whether its effects upon downtown real estate values can yet be very clearly defined. Widening of streets, substitution of busses for street cars, one-way thoroughfares and more parking lots could conceivably reverse, or at least arrest this trend," says Mr. Keidel, Jr. He is manager of the mortgage loan department of Piper & Hill of Baltimore.***

"It all comes down primarily to a consideration of *local trends*. To what extent is the appraiser justified in predicting this trend and how should he deal with it in his report? *First*, an analysis of the city is essential—an appraisal of it as an economic entity. The report should give principal industries, their stability, growth or decline and the responsible factors. The Chamber of Commerce can always supply abundant material on these subjects: Number of new industries, size and trend of payrolls, and numerous indices which have a bearing on the growth or decline of the city and the geographic distribution of prosperity in the metropolitan area. Some of these are new telephones connected, new gas meters, department store sales, number of passengers carried by public conveyances, building activity curve, and rents, vacancies and foreclosures. Important too is the financial condition of the city as it controls the tax rate. High taxes not only discourage new industry, but often are responsible for the movement of industries and people to the surrounding suburban areas.

"Supported by this and other collateral data, the appraisal report should state that the community is growing or declining, and whether or not the trend appears to be sound and permanent. Today temporary growth resulting from emergency defense contracts must be very carefully analyzed; and in this respect the judgment and experience of the appraiser is *all important*. However, apart from the effect of war contracts, this study should permit a fairly long-term prediction regarding the city's economic future (always subject, of course, to national

catastrophes such as severe depression, drought, war, etc.)

"Next in the report will come a classification and a description of the particular section of the city surrounding the property under appraisement. Here again, no prediction is possible without a thorough collection of available data. And here is an important point: In dealing with store properties, in those centers where chain stores predominate, today's rents are often a function of *the consumer demand which existed or was in prospect several years ago.* Rents were then based on a certain expected volume of business which may or may not have since materialized. Therefore, it is necessary to determine whether today's profits justify today's rent based on leases made in the past. Here we get back to consumer demand. Future predictions must constantly reflect an analysis of this *fundamental controlling factor.*

"What is the growth pattern of the district? Has residential construction been active or slow? Has the population center shifted? And will present and contemplated new building accentuate the shift? Are transportation and parking convenient? What competing sites are available? When do important leases expire? The answers to these and many other questions will gradually shape the key to the future trend.

"It's difficult to say *how far* in the future the appraiser is justified in predicting. Downtown business sections of large cities, being well anchored, are the most stable and hence the most predictable. Outlying or neighborhood sections, although consumer demand may be fairly well defined, are more susceptible to shifting, and not so well established as to prevent the growth of new and competing facilities.

"Some may feel that this assumption is no longer true because of the decentralization which is taking place in large metropolitan areas. We all recognize this movement, and the causes for it are fairly obvious. However, it is a *relatively recent development;* and I doubt whether its effect upon downtown real estate values can yet be very clearly determined. Widening of streets, substitution of busses for street cars, one-way thoroughfares and more parking lots could conceivably *reverse, or at least arrest, this trend.*

"In his report the appraiser should be as definite in forecasting future trends as he has facts to support such conclusions. Usually, the larger and the more established the district, the more data available—and hence the more confidence he can express in the future. *I do not believe that an appraiser is either expected to or justified in stating that certain conditions will prevail for, let us say, five years or ten years.* Rather should he emphasize the decisiveness and direction of the present trend (or the lack of it) by the conclusiveness of his supporting data. His report should attempt to achieve as concrete a determination as possible of the direction of the present trend of values rather than a statement that a certain set of conditions will prevail at some future date or for a certain specified term of years.

"I DO not believe that an appraiser is either expected to or justified in stating that certain conditions will prevail for, let us say, five years or ten years. Rather should he emphasize the decisiveness or direction of the present trend (or lack of it) by the conclusiveness of his supporting data."

—Albert Keidel, Jr.

"Once having determined the trend, it will affect the value estimate in several ways in the course of processing the gross income to be expected from the property. It may appear to some degree in one or all of the following items: (a) The vacancy estimate; (b) The various expense estimates, particularly taxes; (c) Obsolescence; and (d) The capitalization rate.

"The last is probably the most important. The appraiser must be able to justify each one of the above figures used in the light of data previously given in his report and should take pains to connect these final conclusions with the proper supporting data."

James D. Picken of the New Jersey Realty Company of Newark, N. J., looks at the same subject—to what extent should an appraiser attempt to predict the future and how should his opinions be treated in the report?

But Mr. Picken doesn't confine himself to income producing properties, but looks at the matter from the broad general angle. He says:

"Appraisers, in valuating property, attempt to estimate the worth of all of rights of all future benefits to the property. Theoretically the benefits accruing from real estate lie in the future. They can't be computed with absolute accuracy; but an estimate of the future probabilities in their relation to the problem is imperative. It would be dangerous to assume that past or present conditions alone indicate the future.

"The future can only be an opinion and this must be based upon a study of past and present conditions and trends. The task of the appraiser is to ferret out what the probable future income or yields may be during the economic life of the property.

"If all pertinent factors and the relationship between all characteristics of a property, as well as the requirements of the owner and tenants are considered proper, the problem then is to find out whether any actual or contemplated neighborhood changes or trends might reasonably be expected to change the situation and increase the risk in ownership or investment.

"Some of the factors that should be considered in the future of residential properties are changes in zoning ordinances, expiring restrictions, lack of proper maintenance in the district, a change of occupancy in neighboring properties to people of different race, or lower living standards. There may be other influences tending to increase sales resistance such as inadequate transportation, a predominance of outmoded architecture, or conditions in a municipality that might indicate a substantial increase in taxation. These, and other factors, will affect the future value of residential properties; and all of them should be considered by the appraiser.

"In apartment properties *the location is important.* The type of accommodations, the rent paying ability and other requirements of prospective tenants must be studied in considering the future. Proposed construction of more competitive buildings in the area, or the shifting of a certain income group from one district to another would have an effect upon the future trend of a locality.

"In commercial properties, a comparison of the past and the probable future of the business area require a study of the neighborhood, land uses, and factors that influence the expansion and trend of business development. Business areas can be seriously affected by the migration of residential population through the development of new communities as well as changes in the purchasing power of the surrounding population.

"The appraiser should attempt to estimate the future benefits of the property *for the remainder of its economic life.*

"In computing value by the income capitalization approach, the appraiser's

(Continued on page 3, column 3)

Should the Appraiser Know the Purpose of the Appraisal Before He Begins?

You must know what kind of value you want but beyond that the less known about the purpose the better

By HUNTER MOSS

SHOULD appraisers know the purpose for which the appraisal is to be made before they start work? First, let's look at it from the appraiser's viewpoint. Then let's see what the question looks like from where we stand—as mortgage brokers making appraisals in connection with mortgage loans in which we are interested.

From the appraiser's point of view it is essential that he know for what purpose the appraisal is to be used before he begins his work. Even though the outcome to an appraisal is *value*, there are a number of different *types of value* that can be reached.

Most of us appraise real estate to find *fair market value* which roughly defined is "the amount expressed in terms of money which a purchaser would be justified in paying for a property, assuming he were to acquire thereby all the rights and benefits to the equivalent extent possessed by the owner."

But in many cases appraisals are made to determine other forms of value. Public utility properties are appraised for *fair value*, which is the base upon which service rates and charges are fixed. Fair value includes such factors as original cost, cost of reproduction today and accrued depreciation, but does not include profits from operation since these are to be determined from the fair valuation.

City, county and state governments use a term known as *assessed value* which all taxpayers would like a definition of. In Cook County, Illinois, for example, it has been reduced to a working formula to give some degree of fairness but in most cases it is the assessor's *guestimate* of market value minus the taxpayer's objection because "John Jones was assessed for $1,000 less than I and his house cost $2,000 more."

Insurance value, another type, is a determination of the base upon which a property may be fairly insured. It makes no consideration of income but is merely an analysis of the bricks and mortar.

There are many other types of value such as *forced sale value*, which is the price that could be obtained at immediate sale, *nuisance value*, *salvage value*, *scrap value*, *book value* and many others.

"HAVE you ever played 'ghost' with your old appraisals? Thumbing through your old files you come across a valuation and wonder 'How did I ever arrive at that one?' Sometimes it was due to bad analysis of the facts, sometimes it was due to an unconscious prejudice for, or against, the neighborhood, block or street; or sometimes it was an unconscious prejudice brought out by a knowledge that a two-thirds loan of $15,000 would be $10,000 and this mortgage application DID HAPPEN to be $10,000," says Mr. Moss. He is with The Moss-Rouse Company of Baltimore, a member of MBA.

All of these value types may be synonymous with fair market value but most often they are not since they assume special circumstances and conditions. Therefore an appraiser must be informed for what purpose his appraisal is to be used before he can attempt the approach to an appraisal.

There is, however, another side to this problem which suggests this question: "With the knowledge that a certain type of appraisal is to be made, should the appraiser know for what purpose it is to be used?"

Some mortgage men use the one-appraisal system and others use the two-appraisal method, the second part of the latter method being of course the independent appraisal.

I was recently talking to a man who works under both systems. He said that, even though he tries to be fair and impartial both ways, he usually ends up being *conservative* in the one-appraisal system. This, he says, is due to the responsibility he knows the company he represents places on him in making loans from his appraisals. These same circumstances might work in reverse with one who did not feel the same responsibility.

The very fact that this man does not appraise exactly the same (depending on whether he is being checked or not being checked) is an indication that in determining a certain type of value it is better to have no knowledge of the circumstances surrounding the appraisal.

Have you ever played "ghost" with your old appraisals? Thumbing through your old files you come across a valuation and wonder, "How did I ever arrive at that one?" Sometimes it was due to bad analysis of the facts, sometimes it was due to an unconscious prejudice for, or against, a neighborhood, block or street; or sometimes an unconscious prejudice brought out by the knowledge that a two-thirds loan of $15,000 would be $10,000 and this mortgage application *did happen* to be $10,000.

It's like brandy in an open decanter. We do not drink it, but you can not help smelling it. It would be much easier if it was not there at all.

Yes, you have to know what kind of value you are to arrive at, but *beyond that the less knowledge the better concerning the purpose of the appraisal*. Appraisers are like teetotalers in one respect. In spite of professed high-mindedness they are human after all.

MEASURING THE FUTURE

(*Continued from page 2*)

first concern is gross income. The amount of this gross is based upon a study and analysis of rentals and other data. The result reflects the appraiser's opinion as to future income.

"The appraisal report should state the conclusions and assumptions of the appraiser and set forth the facts and opinions upon which they were based. These, together with the final value estimate, reflect the judgment and opinion of the appraiser in regard to the future of the property as of the date of his appraisal."

Let's Explore Mutual Mortgage Insurance for Farm Loans

A new day in farm mortgage lending might result from adoption of this plan, says this Utah mortgage banker

***By* FREDERICK P. CHAMP**

MUTUAL mortgage insurance, if applied to farm mortgages under the program previously outlined in these columns, could be expected to bring to farm borrowers in sound agricultural regions of limited area the benefits of *additional* credit. To institutional lenders it would bring the advantage of making investments in districts which heretofore have offered too limited volume to make acquisition costs under conventional lending reasonable.

There are many choice farm areas in the irrigated valleys of the West where water rights are proven and stabilized, which offer the farm mortgage lender a most desirable outlet for his funds. The necessity for accurate appraisal of water rights and varied soil conditions common to mountain areas, when accompanied by a limited volume of available loans, has presented a problem to large institutional lenders. In many instances they have preferred to remain in regions which offer larger volume and more uniform agricultural development.

The high and uniform standards of appraisal requisite to any sound system of mutual mortgage insurance lending should tend to overcome this retarding factor and give the investor added geographical diversification.

Furthermore, the restrictions imposed upon approved originating mortgagees would remove the common hazard—magnified in such areas—which accompanies competition for the limited volume of available business by branch offices, correspondents, agents and government agencies. These agencies frequently apply varying standards of appraisal and may lack a well-grounded knowledge of the factors underlying farm values in fields of limited area as well as resources and personnel adequate to properly service scattered loans. The institutional lender would still have the option of selecting these districts of limited volume, or any other districts, after applying its own standards of evaluation of all the factors operating for or against sound investment opportunity.

They would have reasonable assurance that once they entered a district there would be a continued application of appraisal procedure grounded on dependable productive standards. The insurance fund would provide a safeguard not now available to cushion the occasional error of judgment or the use of undependable information which occurs where lack of volume has decreased the opportunity for experience and comparison.

IN this article Mr. Champ explains the advantages, as he sees them, in the proposal to seek legislation which would mean applying mutual mortgage insurance to farm mortgages. He is a member of the MBA Farm Loan Committee and, with Past President S. M. Waters and R. O. Deming, Jr., has been active in exploring this idea. He is president of the Utah Mortgage Loan Corporation of Logan, Utah, and vice president of the Mortgage Bankers Association of America.

The complaint now raised by the borrower and others that the present private system of farm lending excludes many districts because of their size and the lack of opportunity to apply mass lending procedure on a comparatively low acquisition cost basis, would be met and the trend to socialization of credit retarded.

I am personally familiar with many well-developed farm districts of limited area or comparative isolation and occupied to a limited extent by local lenders. These districts do not appeal to the larger private institutional lenders because of the expense of investigation or re-inspection, or the lack of protection. It seems to me that a well-organized system of reappraisal under the supervision of a government agency should offer this protection in some measure at least.

At any rate, it appears that with the narrowing margin of profit in the farm loan business, this particular aspect of the problem is not likely to be attacked successfully by *individual lending agencies,* each acting independently, and with the resulting duplication of effort and expense. In all parts of the country there are still farming areas in which the long-term lending of investment funds cannot be undertaken without undue risk. As in the past, these areas must be left by prudent lenders to the attention of government agencies operating on a *relief basis.*

The doubtful social benefits attached to subsidizing these districts with public funds is a question which is likely to receive social and political, rather than economic appraisal. But it is less likely that pressure for the extension of credit to such areas will creep into a voluntary system of lending private funds under a government supervised mortgage insurance system than into a system of direct government lending—or even direct private lending—which lacks the double-check provided in the discretionary right of the private lender and the obviously more clear-cut supervisory responsibility inherent in the custodianship of a mortgage insurance fund.

In short, it is believed that farm lending under a well conceived system of mutual mortgage insurance, *should expand the desirable loaning territory available to the institutional lender.* It should afford a means of re-entry of private capital on a substantial scale into good districts now largely served by government lending agencies or local private funds of limited volume.

It is also reasonable to assume that any well conceived and operated system of farm mortgage lending under mutual mortgage insurance would accelerate the lending of local private capital in the farm field and thus *supplement* the funds of larger institutional investors. Historically, no industry has greater stability than agriculture. There can be no sound reason for excluding this basic security and this industry of basic production from any well-rounded scheme of credit

extension in a profit economy. To do so would be an admission of defeat on the part of the American mortgage banker and business man and a reflection upon his ingenuity and resourcefulness. Defeat in this important field can only presage retirement elsewhere, as the *same fundamental principles* operate ultimately in all fields of mortgage lending.

Direct government subsidy of farm credit will, in my opinion, lead to direct government subsidy of other forms of credit. A government credit monopoly in one field will inevitably lead to similar experimentations in others. Complete socialization of credit is apt to be the result, if not the objective. On the other hand, a determined effort to find the answer to this problem of putting the basic security of the land *back in the capital market* would not only delay or permanently defer the evil day, but would put to work investment funds now idle. It would actually provide credit not now readily available, and serve the *national* interest in other ways.

Today when our concern is first with national defense, it is more than ever apparent that the national interest can best be served by releasing federal funds, commitments and credit now involved in the conduct of any normal peace-time activity for use in the all-important wartime or defense functions. If private capital can be used to a larger extent, as it should be, in the normal or even routine long-term financing of agriculture through the instrumentality of the farm mortgage, the federal credit now involved in subsidizing government farm mortgage lending agencies could be released for the vital needs of financing rearmament. Not only would any strain on the federal credit be lessened to the extent of a reduction in its present commitments in the farm mortgage field, but, what is of even greater importance, the further involvement of the federal government in this peace-time credit function could be avoided at a time when every domestic consideration should be subrogated to the financial and the industrial needs of defense.

Incidentally, the sound re-employment of private investment funds in the farm mortgage field would increase the national income and reinforce the ability of our investing taxpayers—whether mortgagees, savings depositors, or insurance policy holders—to carry and liquidate the burden of government debt resulting from our rearmament program. The increased encroachment of government in this fundamental investment field would further sterilize the available investment dollars which represent the savings of the people.

If there is any basis for these suggestions, *should there be any hesitancy on our part* in thoroughly exploring the possibility of applying to the farm mortgage field the principles of mutual mortgage insurance now being used in the home lending field?

Under a mutual mortgage insurance plan in either field *private capital is loaned;* there is *no involvement* of government funds or credit beyond the operation of the mutual mortgage insurance administration. This, in turn, is designed to be self-sustaining and which, under any eventuality or reasonable expression of the public will, would not involve the government beyond the redemption of guarantees on distressed mortgages insured thereunder. Furthermore, the cooperative aspects of mutual mortgage insurance, which appeal to the cooperative-minded borrower, would be introduced into and accompany the employment of private investment funds in the farm loan field.

Although competition of other forms of lending is restricted and interest rates are stabilized (if not, in effect, regulated), the free right of selection of risk by the lender is retained and there is at least a practical distribution of the risk. The questions of interest rates, ratio of loan to value, insurance costs, term, etc., are questions difficult to resolve in the present money market and with the lack of precedent and experience except that developed in the residence loading field by FHA.

However the time is ripe, in my opinion, for a thoroughgoing and realistic consideration of this subject by the institutions and agencies either concerned

(Concluded on page 7, column 3)

CAPITALIZATION METHOD AND APPROACH IN 80-100% LOCATIONS OF ONE-STORY COMMERCIAL PROPERTIES

By **Frank D. Hall**

Chief Appraiser, The Equitable Life Assurance Society of the United States

WHAT is the approach and method of capitalization in 80 percent to 100 percent locations of one-story commercial properties? First, establish, by a comparison of current rents in similar locations, a fair rent if the property had to be rented to a new tenant, other than one of the national chain stores (without regard to the actual rent) less about 5 percent for vacancies and losses. Call this the stabilized effective gross income.

Next, deduct therefrom:

(a) A sum sufficient to pay the estimated annual taxes considering present tax and probable trend in local taxation;

(b) The fire insurance annual premium;

(c) A sum estimated sufficient, if spent annually, to maintain the property in good condition, probably about 1 percent of the building replacement cost;

(d) About 5 percent of the rent for management and rental commissions; and

(e) A reasonable reserve for depreciation.*

Third, capitalize the net remaining at a rate sufficient to attract buyers which today seems to be about 6 percent.

Fourth, if the property is leased for a term at a rental lower than the stabilized, deduct from the capitalized value above, the present worth of the rental deficiency at 6 percent per annum for the full term of the lease.

Fifth, if the property is rented to a responsible tenant at a rental higher than the stabilized, add to the capitalized value above (3) the present worth of the excess rents guaranteed under the lease, for the firm term thereof only, and not over 20 years, at a rate not less than 6 percent for tenants commanding the highest credit rating such as Woolworth, Sears Roebuck, Penney, etc. The rate is to increase to 7 percent or 8 percent for terms beyond about 20 years and increases also as the credit responsibility of the tenant decreases.

Sixth, any surplus value attributable to the surplus income (5) distribute as follows: From the total value, give to the building the full replacement cost of the usable portions thereof less actual observed depreciation. To the land, give the residue, qualifying both values "as benefited by the lease."

*The weak link in the formula, as in any capitalized process, is the reasonableness of the depreciation reserve. Buildings of this type do not change much in style other than the fronts which do not involve much structural change and the more likely depreciation is economic rather than physical or functional. The economic life is reasonably certain to be less than its physical life but any estimate thereof approaching precision is impossible. Most appraisers use about 2 percent of the replacement cost and let it go at that.

Next MBA Clinic April 5th in Cincinnati

MBA's 1941 Clinic program reached the half-way mark with the Chicago meeting February 15th. It was the largest Clinic so far with attendance reaching nearly 250. Fifty-five cities in 25 states and the District of Columbia were represented. Chicago registrations totaled 70. Des Moines sent 7, Detroit 12, Minneapolis 10, Kansas City 8, St. Louis 11, Cleveland 9, and Milwaukee 16.

The next Clinic is scheduled for Cincinnati April 5th and the final meeting will be held shortly after that in Dallas. More about them later.

Property Management was on the Clinic table. Which functions best—the small office or the highly specialized one? L. D. McKendry of Chicago had opened up the matter when he said that sometimes the best results are secured from the small office. Carlton Schultz seemed to sum it all up pretty well when he concluded that,

"It's all a matter of personnel. If you have six or sixty no-good men you still have nothing. Good property management is a matter of getting the right men to manage the properties."

Wonder who raised that *lone* hand when Harry A. Fischer of Chicago asked how many approved the proposed increase in FHA loans from 90 to 95 percent? One man who has talked with Washington officials in recent weeks de-

(Continued next page, column 2)

THESE MANAGED THE CHICAGO CLINIC: Left to right, Hugo Porth, Milwaukee, who led the Service Costs discussion; Claude A. Campbell, Toledo, who led the discussion on Acquisition of New Business; Dean R. Hill, Buffalo, MBA President; C. A. Mullenix, Cleveland, MBA's Central Regional Vice President who was in general charge of the Chicago Clinic; Carlton Schultz, Cleveland, who led the discussion on Property Management; and Charles H. Sill, Detroit, who led the discussion on Appraising. Harry A. Fischer, Chicago, who led the FHA discussion, was not present when this photograph was taken.

THE CHICAGO CLINIC AS THE CAMERAMAN SAW IT: The view is from the right of the rostrum and most of the nearly 250 who attended are shown in this picture. The Clinic opened promptly at 10 and continued until 5:30.

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DEAN R. HILL........................*President*
FREDERICK P. CHAMP........................*Vice President*
GEORGE H. PATTERSON................*Secretary-Treasurer*

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MARCH 1, 1941

FOOD FOR THOUGHT

Dan C. Crane, secretary, The Land Title Guarantee and Trust Company, Cleveland, puts his finger on a pretty vital operating problem in mortgage banking when he says:

"It seems to be the general opinion that it takes at least ¾ of 1 percent servicing fee to in any way cover the cost of properly servicing a mortgage.

"It is my feeling that at present agents are selling mortgages for a premium and, in order to help the sale, they take the servicing of the mortgage at too small a fee as they are anxious to sell the loan.

"In other words, they are lumping both the sale and servicing under one head, when actually they are two different operations. It is as if a firm selling an automobile would agree, after the sale, to service the car below cost.

"The only thing that I can see that will remedy the situation is that the sale of mortgages must stand on its own and the servicing contract be treated as an altogether separate instrument with the servicing agents receiving an appropriate amount for their services."

The Factors That Determine Real Estate Development

"THE economic strength in a community sets the limit of demand and should serve as a guide in real estate development and investment. It is economically sound to assume that if construction *exceeds the needs of a community,* there would follow shortly a break in values.

"The stability of proposed or existing residential communities or business centers should be ascertained as to *permanency of occupancy and earning power.* The changing of residential areas from a high income group to a lower, or vice versa; or to a different nationality or color, should serve as a warning that future values are *likely to be affected.* These elements should be carefully weighed when making an appraisal to be used as a basis for long-term mortgage investments. Neighborhood trends should be controlling factors, and should be stated clearly when rendering an opinion as to the fair value of any property. The trend toward decentralization of long-established business areas is also a problem, and should be considered in all opinions of value. Zoning regulations and traffic problems appear to me to exaggerate the need of decentralization, and should be corrected before it can be stated definitely that the economic necessity for removal to outlying areas exists.

"Mortgage men should be careful not to permit the term 'fair value' to be determined by the abnormal demands created during the period of preparation for national defense. Stimulation of this type leads to disaster when the need ceases to exist. Such stimulation, many times in the past, has reached boom proportions, and carried values far above the economic strength of the community. 'Fair value' *can be fair value* only when *reasonable and consistent* with all of the known facts."—**A. C. Houghton, president, E. Quincy Smith, Inc., Washington, D. C.**

NEXT MBA CLINIC

(*Continued from page 6*)

clared he didn't think the bill making this possible had much chance. He said he understood FHA officials didn't think highly of the plan.

END OF CHAMP ARTICLE

(*Continued from page 5*)

directly now or potentially as future operators with farm mortgage lending or with the investment of mortgage funds in any field. The alternative may be a further surrender of the basic security of the land to government lending and further encroachment upon the field of private enterprise in this country to the ultimate detriment of all.

THE CANDID CAMERA catches (left to right), J. J. F. Steiner, Birmingham, William B. F. Hall, manager of the mortgage loan department of The Lincoln National Life Insurance Company, and Edward D. Auer, assistant manager of the department. Mr. Auer spoke on the type of information a loaning executive wants from an appraisal report. You'll read it soon, in article form.

LISTENING TO THE DISCUSSIONS were (left to right, foreground), Frederick P. Champ of Logan, Utah, and S. M. Waters, Minneapolis, members of MBA's Farm Loan Committee which held a special meeting the day before the Board of Governors meeting. Left foreground: Frank J. Mills of Ft. Wayne, Indiana.

What Value Has Educational Advertising for Mortgage Houses?

Interesting people in home building and home buying rather than in your firm's services has been profitable

By W. W. SLOCUM

I AM a firm believer in educational advertising as a producer of mortgage business, if done at the *proper time* and under the *proper circumstances.* This has been proven by the results of the educational advertising programs conducted by our institution. Of course, times change and the plans used four or five years ago are out of date. An entirely new set of conditions prevail.

Our experience runs something like this. People are *always* interested in new homes. *Most* new homes require new loans. Early in 1935 the FHA was just getting started in Detroit. Few people knew much about it. Only a limited amount of publicity had been given the plan. We investigated it carefully and found it embodied the *same plan* which we have used since our bank started 38 years ago, namely, a monthly payment loan including principal and interest. We found that FHA had done what we had always wanted to do—include the hazard insurance and taxes in the monthly payment. We saw that this type of loan was *tailor-made* for us. We immediately announced that we had $5,000,000 available to build new homes in metropolitan Detroit under the FHA plan.

A booklet was prepared containing the principal information regarding the FHA plan and written so that the prospective home owner could understand it. It carried illustrations of homes on which we had made loans and a schedule of monthly payments for loans of different amounts. We also did some newspaper advertising at that time and found that people were eager to secure information about how they could own a home of their own on payments which approximated the amount of rent they were paying. These booklets were used very effectively at our booth at the Detroit Builders Show that year.

Again, in the early part of 1938, we prepared and published a book of small homes with floor plans. We felt that the time had arrived when the small home was to be popularized. The FHA early that year liberalized their terms to stimulate this type of building. People were again anxious to secure information about homes; this was proven by the fact that we were required to duplicate our order for 10,000 of these booklets. Results in loans far exceeded our expectations. We again used this booklet with excellent results at the Builders' Show booth, where we exhibited illuminated, enlarged, colored photographs of homes on which we had made loans.

WHEN FHA came along, the plan it offered was exactly what the author's bank had always wanted to offer—a monthly payment loan (the kind it had been making for nearly four decades) but with hazard insurance and taxes included. They immediately began educational advertising—the kind in which you seek to interest people in real estate, in new homes, etc., rather than in the services your firm has to offer. It paid dividends to the United Savings Bank of Detroit of which Mr. Slocum is president.

By the end of 1938 we found *a change was taking place.* The papers had fully publicized FHA and its advantages. Small home building was starting in earnest. Builders were selling homes from models, which was much more effective than selecting them from plans and specifications or from booklets. Our booth, the next spring at the Builders' Show, displayed colored drawings and floor layouts of small homes which were submitted by different architects in our city. These homes were actually built, all on one street for display purposes, by builders of the Greater Detroit Builders Association; and many homes were sold from these models.

We have always believed that newspaper advertising produces the best results for the least expense. All other forms of advertising media are supplemental and they're all good if the advertising appropriation is large enough to include them. In the early years after the depression and at the time the FHA was starting, newspaper advertising produced very satisfactory results for us. Times, however, have changed; competition in Detroit has become so keen for mortgage loan business that it almost seems there are more brokers and solicitors than loans. A loan applicant is almost appalled by the solicitation he receives from mortgage brokers when it becomes known he is considering building a home. Solicitors camp on the prospect's doorstep like a baseball fan waits at the box office in the early morning before dawn, to purchase tickets for a World Series. *To attempt to attract a large volume of new mortgage loan business through newspaper advertising, in a competitive market of this kind, is almost futile.*

However, we feel that newspaper advertising still provides the best advertising medium commensurate with its cost. The excellent real estate sections of our Sunday newspapers provide the educational interest which always attracts those who are thinking of building or buying homes. People want to know about the new homes, new home construction and new conveniences; and it is only natural that they would turn to these sections of the papers. This is also true of people who are planning new improvements for homes already built. That the builders feel newspapers are an excellent medium for advertising their new homes is attested by the fact that the real estate sections of the Sunday papers are filled with advertisements containing illustrations and prices of new homes offered for sale.

Irrespective of the business brought in by brokers, we feel that a considerable proportion of our new mortgage business coming directly to us, is the result of newspaper advertising.